TRANSCRIPT OF PROCEEDINGS

FEDERAL HOUSING FINANCE BOARD

OPEN MEETING

Pages 1 thru 35

Washington, D.C.
July 10, 2002

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FEDERAL HOUSING FINANCE BOARD

OPEN MEETING

Wednesday, July 10, 2002
Washington, D.C.

The Board meeting convened, pursuant to notice, at 10:00 a.m., at 1777 F Street, N.W., Second Floor Board Room, Washington, D.C.

PARTICIPANTS:

JOHN T. KORSMO, Chairman

J. TIMOTHY O'NEILL, Director

FRANZ S. LEICHTER, Director

JOHN C. WEICHER, Director

ALLAN I. MENDELOWITZ, Director

JAMES L. BOTHWELL, Managing Director

ARNOLD INTRATER, Acting General Counsel

ELAINE L. BAKER, Secretary to the Board

SCOTT SMITH, ACTING DIRECTOR, OFFICE OF POLICY, RESEARCH, AND ANALYSIS

THOMAS HEARN, SENIOR ATTORNEY-ADVISOR

THOMAS JOSEPH, SENIOR ATTORNEY-ADVISOR

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AGENDA

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Consideration of approval of the Federal Home Loan Bank of Indianapolis' Capital Plan and related resolutions

P R O C E E D I N G S

CHAIRMAN KORSMO: Good morning. I call this meeting of the Federal Housing Finance Board to order. We have before us today three capital plans from the Federal Home Loan Banks of Des Moines, Topeka, and Indianapolis, and we will be taking them in that order if there's no objection.

For those of you from the Banks who are either here or are watching on the Internet, good morning to you, as well. I know Andy Jetter from Topeka is here and I know Jonathan West from Indianapolis is here, there may be others from any of the three Banks, we certainly welcome you here today as we take a look at your Capital Plan proposals.

The Capital Plans we have before us represent many months of diligent and dedicated work by the staffs of both the individual Banks and the Finance Board. I appreciate the cooperative attitude everyone has displayed during this lengthy and complicated process.

These are the 9th, 10th, and 11th Capital Plans the Finance Board has considered, leaving just the Plan of the Federal Home Loan Bank of New York, which we will consider at a special meeting next week in New York City. I hope as many as possible can be there for that meeting.

I should mention the meeting in New York next week will not be Web cast, either simultaneously or subsequently due to the cost. So I apologize for that, however, we look forward to an interesting and a good meeting in New York and I hope that as many people as possible can participate in that session.

The Board's consideration of these Capital Plans has been open and thorough, with any disagreements stated clearly and on the record, as they should be.

As we reviewed and approved the eight plans so far, one thing has become apparent: these Plans have been shown to be safe, sound, and legal. By far, the Board's most important considerations in reviewing the Plans.

But they've also demonstrated at times unique differences from one another, reflecting varied business judgments made by each individual Bank. That is, I believe, entirely consistent with the language and intend of the Gramm-Leach-Bliley Act, which has governed our process.

The Act stated--and the exact language is worthy of note: "The Board of Directors of each Federal Home Loan Bank shall submit for Finance Board approval a Plan establishing and implementing a capital structure for such Bank that the Board of Directors determines is best suited for the condition and operation of the Bank and the interests of the members of the Bank."

The statute charges the individual Banks, not the Federal Housing Finance Board with preparing a capital plan that best suits the conditions and operation of the Bank and the interests of its members. The directors and management of the Des Moines, Topeka, and Indianapolis Banks have submitted Plans to us they believe meet these statutory criteria.

Our obligation today, as in past considerations is to determine whether they are safe, sound, and legal. And with that admonition, I will call on our Managing Director, Dr. Jim Bothwell to introduce the Agenda.

MR. BOTHWELL: Thank you, Mr. Chairman, and good morning to you and all members of the Board.

As you mentioned in your opening remarks, Mr. Chairman, there are three proposed Bank Capital Structure Plans on today's agenda: the Capital Structure Plan for the Federal Home Loan Bank of Des Moines; the Capital Structure Plan for the Federal Home Loan Bank of Topeka; and, the Capital Structure Plan for the Federal Home Loan Bank of Indianapolis.

Each of these three plans on today's agenda, Mr. Chairman, involve three related resolutions. The first of these resolutions approves the Bank's Capital Structure Plan subject to the bank's receiving the required Finance Board approvals of their internal market-risk models and their risk-assessment procedures and controls before implementation can occur.

The second resolution specifies the provisions of the Finance Board's existing Financial Management Policy that the Banks would still be subject to upon implementation of their new capital structures.

And the third resolution, Mr. Chairman, waives the six-month notice requirement for redeeming the Bank’s existing stock, thus allowing the Bank to convert more rapidly to their new, permanent risk-based capital structures.

And without further adieu, at this time, Mr. Chairman, I would like to ask Scott Smith, the Acting Director of the Policy Office, accompanied by Tom Hearn from the General Counsel's Office to present the first of the proposed Capital Structure Plan for the Federal Home Loan Bank of Des Moines for the Board's consideration; followed by the Capital Structure Plans for the Topeka and Indianapolis Banks. Scott.

MR. SMITH: Thank you, Jim. Good morning, Mr. Chairman and Members of the Board. Staff is requesting that the Board of Directors consider and approve three resolutions that are concerned with and constitute approval of the structure component of the Des Moines Bank's Capital Plan.

The Finance Board staff finds that the most recent version of the Plan, approved by the Bank's board of directors on July 8, 2002, complies with Finance Board regulations. The structure of the Plan, essentially, is a continuation of the capital structure currently in effect, but with modest adjustments.

The Des Moines' Plan provides for Class-B stock only, with two subclasses: one for membership stock and one for activity-based stock. Because it is an all Class-B stock structure--and based on staff estimates--the Bank will meet the 4 percent leverage requirement for un-weighted stock and the 5 percent weighted stock leverage requirement upon conversion and also will meet the risk-based capital requirement.

At this point in time and going forward, staff believes that the leverage requirement, rather than the risk-based capital requirement will be the binding constraint on the Bank's minimum capital.

If approved, the Bank intends to convert to the new capital structure in 18 months or less. Implementation of the Plan will position the Bank with more permanent capital and will require that the Bank adopt a more state-of-the-art risk-management process.

Under the Capital Plan, a member's minimum investment requirement is equal to the sum of a member's membership stock requirement and it's activity-based stock requirement. The membership stock requirement equals .12 percent of a member's total assets, subject to a cap set at $10 million and a minimum set at $10,000.

The range within which the member's membership stock-purchase requirement changes--percentages can be changed without approval of an amendment is set at .1 percent to .25 percent.

The activity-based stock-purchase requirement is calculated based on the outstanding balances of specific transactions associated with the member and carried on the Bank's balance sheet.

The percentages are initially set at 4.45 percent for advances; 4.45 percent for acquired member assets AMA; .15 percent for letters of credit; and 0 percent for advances in AMA commitments.

The Plan also provides ranges for these percentage amounts. The ranges for both advances in AMA are from 3 percent to 5 percent.

Finance Board rules provide that the minimum stock-purchase requirements established by a Plan must be set at a level that provides sufficient capital for the Bank to comply with it's minimal capital requirements. As part of this analysis, staff reviewed materials submitted by the Bank to support approval of the Plan, including pro forma financial statements, the assumptions behind these statements and management's estimates of the amount and type of stock that would be associated with the pro forma statements.

Staff analysis of the Bank's projections indicate that the Bank will have sufficient capital at the moment of implementation.

Overall, staff has not identified any apparent structural flaws or other problems in the Plan and the initial proposed minimum investment requirements that would prevent the Bank from maintaining sufficient capital to comply with statutory and regulatory requirements and continue to operate in a safe and sound manner.

We would be pleased to answer any questions.

CHAIRMAN KORSMO: Do the Directors have questions of Dr. Smith and Mr. Hearn? Hearing no questions, could the Chairman entertain a motion to approve the three resolutions that pertain the Des Moines Bank's Capital Plan. Dr. Mendelowitz?

DIRECTOR MENDELOWITZ: I so move.

CHAIRMAN KORSMO: It has moved that we approve the three resolutions that pertain to approval of the Capital Plan of the Federal Home Loan Bank of Des Moines. Is there any discussion of the motion? Is there any discussion of the motion? Seeing no discussion, I will call on the Secretary to call the roll on the question of the three resolutions and to adopt the Des Moines' Plan.

MS. BAKER: On the motion before the Board, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. BAKER: Director O'Neill?

DIRECTOR O'NEILL: Yes.

MS. BAKER: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. BAKER: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. BAKER: Chairman Korsmo?

CHAIRMAN KORSMO: Yes. The motion is adopted and the resolution to approve the Capital Structure Plan of the Federal Home Loan Bank of Des Moines; the resolution dealing with waiver of the withdrawal notice requirement;

and the resolution dealing with provisions of the Financial Management Policy -- excuse me, exemption, are adopted. Thank you.

Who am I calling on now, Scott, again? We move now to Item 2 on our Agenda, which is the consideration of the approval of the Plan submitted by the Federal Home Loan Bank of Topeka and related resolutions.

MR. BOTHWELL: And I just note that Scott's being joined by Tom Joseph of the General Counsel's Office.

MR. SMITH: Thank you once again, Mr. Chairman.

Staff is requesting that the Board of Directors consider and approve three resolutions that are concerned with and constitute approval of the structure component of the Topeka Bank's Capital Plan.

The Finance Board staff finds that the most recent version of the Plan, approved by the Bank's board of directors on July 2, 2002, complies with Finance Board regulations.

The structure of the Plan helps implement Topeka's goal of tying the cost-born by a member and the rewards afforded a member more closely to the member's level of activity with the Bank.

The Topeka Plan authorizes the issuance of both Class-A and Class-B stock, although neither class of stock is preferred to the other. The only other Bank to have proposed an A/B structure was Chicago.

Members must hold Class-A stock to satisfy the Plan's membership stock-purchase requirement, which is called the asset-based stock-purchase requirement and Class-B stock to satisfy the Plan’s activity-based stock-purchase requirement.

On the date of conversion, the Bank will convert all member's existing stock into enough Class-B stock to fulfill the member's activity-based stock-purchase requirement. All remaining stock will be converted into Class-A stock.

The Plan also provides the Bank the option to exchange all or a portion of a member's excess Class-B stock, as it comes to be, for excess Class-A stock, provided--

CHAIRMAN KORSMO: It becomes to be excess?

MR. SMITH: --yes, it comes to be excess, sorry--provided that the Bank will remain in compliance with it's capital requirements after the exchange.

Based on staff estimates, the Bank will meet the 4 percent leverage requirement for un-weighted stock and the 5 percent weighted-stock leverage upon conversion and will also meet the risk-based capital requirement.

At this point in time and going forward, staff believes that the leverage requirement, rather than the risk-based capital requirement will be the binding constraint on the Bank's minimum capital.

If approved, the bank intends to convert to the new capital structure in 18 months or less. Implementation of the Plan will position the Bank with more permanent capital and will require that the Bank adopt a more state-of-the art risk-management process.

Under the Capital Plan, a member's minimum investment requirement is equal the sum of a member's asset-based stock-purchase requirement and it's activity-based investment requirement.

The asset-based stock-purchase requirement equals .1 percent of a member's total assets, subject to a cap initially set at $500,000 and a minimum set at $1,000.

The range within which the member's asset-based stock-purchase requirement percentages can be changed without approval or an amendment is set at .1 percent to .3 percent.

The activity-based stock-purchase requirement is calculated based on the outstanding balances of specified transactions associated with the member and carried on the Bank's balance sheet. The percentages are initial set at

4.5 percent for advances; 5 percent for AMA; .5 percent for letters of credit; 2 percent for the notional amount of exchange agreements entered into with a new member.

The range within which a member's activity-based stock-purchase requirement can be changed without approval of an amendment is as follows: Advances 4 to 5 percent; AMA 0 to 6 percent; letters of credit 0 to 1 percent; and exchange agreements 1 to 3 percent.

Finance Board rules provide that the minimum stock-purchase requirements established by a capital plan must be set a level that provides sufficient capital for the Bank to comply with it's minimum capital requirements.

As part of this analysis, staff reviewed materials submitted by the Bank to support approval of the Plan, including pro forma financial statements, the assumptions behind these statements, and management's estimates of the amount and type of stock that would be associated with the pro forma statements.

Staff analysis of the Bank's projections indicate that the Bank will have sufficient capital at the moment of implementation.

Overall, staff has not identified any apparent structural flaws or other problems in the Plan and the initial proposed minimum investment requirements that would prevent the Bank from maintaining sufficient capital to comply with statutory and regulatory requirements and to continue to operate in a safe and sound manner.

Once again, we'd be pleased to answer any questions.

CHAIRMAN KORSMO: Are there any questions for Dr. Smith or Mr. Joseph? Dr. Mendelowitz.

DIRECTOR MENDELOWITZ: I don't have a question, but I do want to note that the recapitalization of the Topeka Bank is the last accomplishment to be realized under the leadership of that Bank by Frank Lowman. Frank retired effective July 1, after 13 years of leadership of the Bank. And I just wanted to acknowledge his many contributions and good service to the Bank and to thank him. And as the Chairman noted, Andy Jetter is the Acting President, currently, and he's with us today. And welcome, Andy, to that capacity and wish him well.

CHAIRMAN KORSMO: Thank you, Allan, for your comment. Are there any other questions of the staff?

DIRECTOR O'NEILL: Not so much a--well, I guess it is a question, but with your talks with the Topeka staff, did you get any sense of why they went A and B when so many others are going only B?

MR. SMITH: The only sense that we have is that this is something that their Board really wanted to stick with. We did talk to them about the option of going all B as many of the other Banks have chosen, but it's simply a preference of their Board.

DIRECTOR O'NEILL: Okay.

CHAIRMAN KORSMO: Any other questions for the staff? Any other questions for the staff? Hearing none, is there a motion to approve the three resolutions involved in approving the Capital Structure Plan for the Federal Home Loan Bank of Topeka.

DIRECTOR O'NEILL: So moved.

CHAIRMAN KORSMO: We have a motion to approve the three resolutions involved in approving the Capital Plan of the Federal Home Loan Bank of Topeka, is there any discussion of the motion? Dr. Leichter.

DIRECTOR LEICHTER: I support the Plan. I do want to state my concern that the range for the capital requirement for required member assets goes from zero to a range of 6. I indicated as we considered some of the other Plans, I feel that unwise in view of the cooperative nature of the System and I think it can raise some safety and soundness issues. I don't believe there are any safety or soundness issues as regards the Topeka Plan. I know the initial requirement for AMA is 5 percent and I don't think that the Topeka bank, like some other Plans, particularly one, envisages a very large AMA activity, so I have no difficulty in supporting this Plan being safe and sound, but I do hope careful consideration will be given before any steps are taken to bring the range for the AMA capital requirement down to zero. I think that would be unwise.

CHAIRMAN KORSMO: Thank you, Director Leichter. Are that any other comments? Any other questions? Any other discussion of the resolutions motion. Any other discussion of the motion? Seeing none, the Secretary will please call the question on the motion to approve the three resolutions involved in approving the Capital Structure Plan for the Federal Home Loan Bank of Topeka.

MS. BAKER: On the motion before the Board, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. BAKER: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. BAKER: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Aye.

MS. BAKER: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. BAKER: Chairman Korsmo?

CHAIRMAN KORSMO: Yes. The motion is carried and the three resolutions, the Capital Structure Plan of the Federal Home Loan Bank of Topeka, the resolution dealing with the Financial Management Policy exemption; and the resolution dealing with the waiver of withdrawal notice requirement are approved; and the Plan is approved.

We move to the final item on our Agenda, which is consideration for approval of the Capital Plan of the Federal Home Loan Bank of Indianapolis. Dr. Smith.

DR. SMITH: Thank you, Mr. Chairman.

Staff is requesting that the Board of Directors consider and approve three resolutions that are concerned with and constitute approval a structure component of the Indianapolis Bank's Capital Plan.

Finance Board staff finds that the most recent version of the Plan approved by the Bank's board of directors on June 28, with technical and conforming changes through July 9, complies with Finance Board regulations.

The Plan authorizes an all Class-B stock structure divided into sub series B-1, and sub series B-2 stock.

The B-1 stock will be converted to B-2 stock if a member files a redemption or withdrawal notice on stock that is required to be held to meet a member's stock requirement.

Excess stock, if any, will not be converted to B-2 stock. The dividend on B-2 stock will be 80 percent of the B-1 stock dividend.

A member's total stock requirement will equal the greater of it's total mortgage assets requirement or its activity-based stock requirement with a minimum investment requirement of $1,000.

The membership side of the "greater of" calculation is 1 percent of total mortgage assets with a cap of $35 million. The Plan includes a range within which the Bank's board of directors can change this total mortgage-assets percentage without amending the Plan. That range is from .75 percent to 1.25 percent.

For the activity-based side of the "greater of" calculation, the requirements are 5 percent for credit products, which are primarily advances; 5 percent for derivative contracts; and 3 percent for AMA.

The ranges are: for credit products, 2 percent to 5 percent; for derivative products, 3 to 5 percent; and for AMA, from 0 to 5 percent.

Based on staff estimates, the Bank will meet the 4 percent leverage requirement and will also meet the risk-based capital requirement on the date of implementation.

At this point in time and going forward, staff believes that the leverage requirement, rather than the risk-based capital requirement will be the binding constraint on the Banks' minimum capital.

If approved, the Bank intends to convert to the new capital structure in 18 months or less. Finance Board rules provide that the minimum stock-purchase requirements established by a capital plan must be set at a level that provides sufficient capital for the Bank to comply with it's minimum capital requirements.

As a part of this analysis, staff reviewed the materials submitted by the Bank to support approval of the Plan, including pro forma financial statements, the assumptions behind these statements, and management's estimates of the amount and type of stock that would be associated with pro forma statements.

Staff analysis of the Bank's projections, indicate that the Bank will have sufficient capital at the moment of implementation.

Overall, Staff has not identified any apparent structural flaws or other problems in the Plan and the initial proposed minimum investment requirements that would prevent the Bank from maintaining sufficient capital to comply with statutory regulatory requirements and to continue to operate in a safe and sound manner.

Once again, we'd be pleased to answer any questions.

CHAIRMAN KORSMO: Are there any questions for Dr. Smith or Mr. Joseph? Director Leichter.

DIRECTOR LEICHTER: Yes, I just want to ask this question of Mr. Joseph. Just to put it on the record because questions have been raised as to one aspect of the Indianapolis Plan, as to whether that causes some problem under the Gramm-Leach-Bliley Act. And I just want to clarify that counsel has determined that the Plan is legal in all respects.

MR. INTRATER: Let me start out the answer, Mr. Joseph is obviously much better informed about all the details, but the short answer to your very appropriate question is that the use of Class-B-2 stock, as proposed by the Federal Home Loan Bank of Indianapolis is legally appropriate. If I didn't believe that, you wouldn't have received a recommendation from staff that you could deliberate to approve the proposed Plan. The Chair would have gaveled down the approvals of the Federal Home Loan

Bank of Des Moines and Topeka and closed the port session, suggesting that the Indianapolis plan was not yet ready for review.

The Indianapolis Plan is unique, in that it provides for a lower dividend to be paid out on the required stock of members that have filed a notice of intent to withdraw from the System.

But the Plan also calls for the same treatment with respect to required stock notice for redemption by a member that is not withdrawing from the System. And we believe that such parity of treatment is consistent with the provisions of 4026.D-1 that members shall be entitled to dividends and other membership rights commensurate with continuing stock ownership. So, as I said the short answer is, Counsel's Office has concluded that the proposal by the Federal Home Loan Bank of Indianapolis as to this issue is legal and appropriate.

DIRECTOR LEICHTER: Good.

CHAIRMAN KORSMO: Any other questions of the staff? Dr. Weicher.

DIRECTOR WEICHER: Have any members indicated a desire to withdraw, do we know anything about the context of this in that sense?

MR. JOSEPH: No. Indianapolis hasn't had a member that has voluntarily withdrawn, at least in the last five years, which is just the date--it might even be longer, so there's no reason to suspect that that will change.

CHAIRMAN KORSMO: Any other questions? Any other questions of staff? If not, the Chair will entertain a motion to consider the three resolutions connected with approval of the Capital Structure Plan of the Federal Home Loan Bank of Indianapolis.

DIRECTOR O'NEILL: I will so move.

CHAIRMAN KORSMO: Thank you. The motion is to approve the three resolutions connected with the approval of the Capital Structure Plan of the Federal Home Loan Bank of Indianapolis. Is there any discussion of the motion? Dr. Mendelowitz?

DIRECTOR MENDELOWITZ: Thank you, Mr. Chairman. We've given a lot of care and attention to the Plan submitted by the Indianapolis Bank in recent days. And I have to observe how pleased I was with the way in which that examination and cooperation in terms of working on the Plan went forward.

For the Home Loan Bank System to operate in a safe and sound manner and fulfill its statutory responsibility requires everyone to do their job. The Banks require good professional leadership and staff. It requires diligent corporate governance and it requires responsible and effective regulation by the regulator. Everyone has to do their job and it's clear, because of recent scandals that everyone does have to do their job.

The regulator cannot sit back and just say the Board of Governors have a statutory responsibility to ensure that the Banks are safe and sound and meet their capital requirements and rely on that. If we could rely exclusively on corporate governance, we wouldn't have had the accounting and business scandals at Enron, we wouldn't have had the scandals at WorldCom/MCI, and we wouldn't have had the scandals at Halliburton.

And so I am always pleased and gratified when I see each level who has responsibility for ensuring a safe and sound system that fulfills its statutory responsibilities and mission are able to work together constructively and productively to ensure a safe and sound system that meets its needs and fulfills it's statutory mission.

And so, I really want to take this opportunity to commend the leadership of the Indianapolis Bank for the very constructive approach that they've taken to working with the Finance Board as regulator in meeting our common objective of a safe and sound Bank Capital Plan. We work together. The Finance Board as regulator articulated what our concerns were. The leadership at the Indianapolis Bank listened with an open mind, with an instructive attitude and, as we went forward, changes and modifications to the Plan were made that certainly met the concerns I had with respect to safety and soundness. Minimum capital charges for derivatives; minimum capital charges for advances and I'd just like to say that the progress made and the willingness to work toward that objective of a safe and sound plan that met everyone's concerns, I think was greatly appreciated. I greatly appreciate it and am pleased with the outcome and want to express my appreciation to the leadership of the Indianapolis Bank.

CHAIRMAN KORSMO: Thank you Dr. Mendelowitz. Is there any other discussion of the motion? Mr. Leichter.

DIRECTOR LEICHTER: Yeah, I think Dr. Mendelowitz well expressed my thoughts on the process which has brought this particular Plan before us and I'm pleased to support it. And I also wanted to express my appreciation to the president of the Indianapolis Bank, Marty Heger and his staff and the board of directors of that Bank, Jonathan West, whose been here representing the Bank and working out some issues that I felt needed to be changed and the willingness on the part of the Bank to make reasonable accommodations so that we do have, at least on advances, a range of capital requirement which doesn't go to zero.

I am concerned that, as I similarly expressed for the Topeka Bank, that on the required member assets that the range can go to zero so that there would be no capital requirement whatsoever for the mortgage purchase activity of the Indianapolis Bank, which I think under their business plan is going to be more significant than some of the other Banks.

Nevertheless, I think if you take a look at their business plan, the fact that they're starting out with a capital charge for AMA activity, I feel comfortable in supporting this Plan. And again, as I did with Topeka, I would certainly urge the Indianapolis Bank not to consider or reach a point where they eliminate all capital charges for required member activity.

But having said that, I think overall we have made the sort of changes or I should say the Indianapolis Bank has agreed to the sort of changes that I think makes this a very good, a very sound and reasonable Plan. And I'm pleased to support it.

CHAIRMAN KORSMO: Is there any other discussion? Seeing none, the Secretary will please call the roll on the question on the motion to approve three resolutions involved in approving the Capital Structure Plan of the Federal Home Loan Bank of Indianapolis.

MS. BAKER: On the motion before the Board, Director Leichter, how do you vote?

DIRECTOR LEICHTER: Yes.

MS. BAKER: Director O'Neill?

DIRECTOR O'NEILL: Aye.

MS. BAKER: Director Mendelowitz?

DIRECTOR MENDELOWITZ: Yes.

MS. BAKER: Director Weicher?

DIRECTOR WEICHER: Aye.

MS. BAKER: Chairman Korsmo?

CHAIRMAN KORSMO: Yes. The motion is approved and the three resolutions approving the Capital Structure Plan for the Federal Home Loan Bank of Indianapolis are approved.

Thank you. I guess, I will join both Director Leichter and Dr. Mendelowitz, and I assume the other members of the Board in thanking the boards and the staff of the three Banks whose plans we considered today and particular thanks to the presidents, Pat Conway from Des

Moines; Marty Heger, from Indianapolis; and Frank Lowman and Andy Jetter from Topeka. We appreciate the hard work that went into making these approvals possible.

In my opening statement today I noted that we are coming to the close of the capital structure approval process. Next Thursday in New York will be the final vote and an appropriate time, I think, to reflect further on what the Finance Board, and the capital plan process have accomplished toward creating a more safe, sound, and secure Federal Home Loan Bank System.

But the Board's work continues, of course, and in the wake of that final approval, we will be turning our attention to other important questions of safety and soundness, as well as governance, and I thank Dr. Mendelowitz for pointing out the direction we intend to move, as well as the many public policy issues that affect the System. While, again, Director Mendelowitz, while I think your listing of scandals and potential scandals is interesting in its selectivity, that notwithstanding, I think you make an important point about the need for all of us to enhance the function that we serve as the regulator of this very important System.

As I mentioned last month, the August meeting will include the consideration of a new standard of conduct governing the arms' length relationship between Finance Board Directors and staff and the Banks.

Another issue we will consider in the months ahead is the System's efficiency in making use of its privileged access to capital markets.

Congress and the investment community provide the Banks with real and presumed advantages allowing them to raise funds at low cost to fulfill the public mission through which the System was chartered. This Board and the taxpayers we serve, I believe, have a right to know the plans and strategies used by the Banks and their agent, the Office of Finance, to make the most efficient and most appropriate use of the public's blessing on the System's debt issuances.

I have no intention of making this process difficult or uncomfortable for the Banks. Obviously, we have no interest in revealing genuine business secrets or unnecessary details about the Banks’ interoperations. Yet, as, again, as Dr. Mendelowitz referred to, yet, in this time of intense focus on accountability and transparency in corporate America, we must stand for the proposition that the public has a right to know at least as much about the Home Loan Banks they guarantee as they do about the publicly traded companies in their retirement funds.

We will not be true to our obligation to protect the public's investment in the Home Loan Bank System if we shield it from public accountability. Each Bank is privately owned, but the value of each franchise is its status and privilege as a publicly endowed enterprise. The public, therefore, along with the public's regulator is entitled to ask questions and seek answers.

I look forward to working with the banks, Finance Board staff and my colleagues to find those answers.

Thank you again, if there are no further comments--Dr. Mendelowitz?

DIRECTOR MENDELOWITZ: Yeah, you alleged some selectivity in my use of examples--

CHAIRMAN KORSMO: I thought that maybe you were jumping the gun on Halliburton a little bit, but--

DIRECTOR MENDELOWITZ: No, and I just want to say that being as absent-minded as I am, I'm usually forced to resort to whatever is most current and this week the three things that were on the front page of the paper were Enron, WorldCom and Halliburton. And that was the only source of choice of what got cited.

CHAIRMAN KORSMO: Point taken.

DIRECTOR MENDELOWITZ: So, but, really, I mean it's--we're sort of, you know, having some light banter back and forth about this, but I really don't want that to detract from what, in fact, is an extraordinary important issue and one that I've identified as an import issue from the very first day that I arrived at the Finance Board, which is the effectiveness and diligence of the corporate governance within in the System.

Having moved from the System post Gramm-Leach-Bliley, in which the boards of directors have greater responsibility for overseeing the safe and sound operations of the Banks, we should, clearly, as you pointed out be focusing going forward on the diligence and quality, effectiveness of corporate governance in the System.

As I've said from the first day I've been here--the first line of defense of a safe and sound System is the board of directors and the quality of the corporate governance. So--

CHAIRMAN KORSMO: As indeed our regs say on that.

DIRECTOR MENDELOWITZ: --and I certainly applaud the focus on that. And one of the things that, you know, it's a good time to talk about ways in which we can enhance that.

One of the concerns that I've had is that because we have 12 different Banks within the System, we don't have a uniform level of practice of the very highest quality, simply because you've got independent Banks doing their own things.

I think one of the really strengths of the System is that when someone does something to that and that becomes the benchmark and the best-in-class, that it provides a vehicle for the rest of the System to learn how to do that very particular activity the very best.

I've suggested on a number of occasions that we might take a new approach to supervision. In addition to the individual Bank examinations that we undertake, I've suggested on a number of occasions that we might undertake a second type of audit, which would be a single-issue, System-wide audit of sort of high-risk or high-important issues in an effort to identify best practices so that we can raise the general level of the System.

And I think maybe one of the first topics for those single System-wide audits would be the exercise of corporate governance within the System so we can identify the best practices with respect to corporate governance and use that examination process as a way of promulgating and informing the System as to what the best practices are and how the System as a whole might do better in this area by emulating the best practices.

CHAIRMAN KORSMO: I appreciate your focus on that issue and I think that our new director of supervision may help us focus for us to consider on exactly that point in the very near future. Director Leichter, did I see your hand up?

DIRECTOR LEICHTER: Yes, it's with some regret that I note that this is the last Board Meeting at which my special assistant, Linda Fleming McGee, will be present. Because I think as most people around this table and in this room know, she is leaving for greater prospects and certainly to spend more time with her son and her family, but I think it's fair to say that Linda's not only been an outstanding help to me, but she hasn't been only my special assistant, I think she has served the Finance Board extremely well and I think she's served the System so I want to publicly express my appreciation and I think that it might be appropriate for the Board also to express its thanks to Linda Fleming McGee for the good service that she's provided.

[Applause.]

CHAIRMAN KORSMO: Your comments, Franz, are not only appropriate, they are necessary, Linda has been a very important to your group. And we're going to sincerely miss you. And I appreciate your raising that point Dr.

Leichter. And I think we're going to acknowledge it again tomorrow. And I'm looking forward to that.

Are there any other comment? If not, as they say in Newark, next stop Penn Station, we'll see you all next week in New York. Thank you. The meeting is adjourned.

[Whereupon, at 10:38 a.m., the meeting was adjourned.]

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